BRIEF IN SUPPORT OF PETITION.

I.

THE DECISION OF THE COURT BELOW ON THE QUESTION WHETHER PETITIONER WAS ENTITLED FOR THE YEAR 1936 TO THE BENEFITS OF THE RELIEF PROVISIONS OF SECTION 112(f) OF THE REVENUE ACT OF 1936 IS NOT IN ACCORD IN PRINCIPLE WITH THE DECISIONS OF THIS COURT AND IS IN CONFLICT WITH DECISIONS OF OTHER CIRCUIT COURTS OF APPEAL.

(a) It is well settled that Section 112(f) of the Revenue Act of 1936 is a relief provision. *Washington Railway & Electric Co.* v. *Commissioner* and cases cited therein, 40 B. T. A. 1229.

A relief provision should be construed liberally to effect its purpose. *Helvering* v. *Bliss*, 293 U. S. 144; *U. S.* v. *Pleasants*, 305 U. S. 357, 363; *Gould* v. *Gould*, 245 U. S. 151.

The Court of Appeals construed this section of the statute strictly rather than liberally and accordingly its decision does not accord with the law as established by this Court in connection with statutory relief measures. The Court below found both as a matter of fact and law that the Gold Street property was acquired for a use similar to that of the Concord Street warehouse which had been owned by the petitioner prior to condemnation. However, the Circuit Court of Appeals decided that the petitioner was not entitled to relief because title to the Gold Street property acquired in place of the Concord Street property was taken in the name of Gold Street Corporation. The Court below relied on the case of *Higgins* v. *Smith*, 308 U. S. 473. We think that *Higgins* v. *Smith*, *supra*, and similar cases involving the creation of corporate entities to avoid taxes have no application to a remedial statute such as Section 112(f) and can have no possible bearing here. There the taxpayer sold securities to his wholly owned self-created corporation at a loss to secure tax deductions. The loss was disallowed by the Court. Here there was no attempt to avoid tax by the formation of the

Gold Street Corporation and the taxpayer in good faith paid over the award money in connection with the replacement of the property.

(b) The Court below followed the form rather than the substance of the transaction involved and held that the petitioner neither acquired the Gold Street property nor the control of the Gold Street Corporation.

The Court below found as a fact that the stock of the Gold Street Corporation, the stock of the petitioner and the stock of Vim Electric Company, the tenant, was owned by the same parties, the Kassover Brothers, in equal shares (R. 68). In its opinion (R. 71) the Court referred to *United States* v. *The Brager Building & Land Corporation*, 124 F. (2d) 349, 351. In that case the United States Circuit Court of Appeals for the Fourth Circuit held that where a corporation was organized for the sole purpose of taking title to real estate for the convenience of a partnership which controlled the corporation, that the income from the property was attributable to the partnership and that the corporation was a mere conduit. In that case the Court followed the substance of the transaction rather than the form.

> "Taxation is not so much concerned with the refinements of title as it is with actual command over the property taxed * * *."
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> *Griffiths* v. *Commissioner*, 308 U. S. 355, 357-8;
> *U. S.* v. *The Brager Building & Land Corporation*, *supra*.

In *North Jersey Title Ins. Co. et al.* v. *Commissioner of Internal Revenue*, 84 F. (2d) 898 (C. C. A. 3), the Circuit Court of Appeals held:

> "Where title insurance company invested in mortgages on vacant lots which were represented as being improved and created subsidiary corporate structure for purpose of dealing with such mortgaged property in order to avoid disastrous results to title insurance business which might follow if public learned of the transactions and not in order to escape taxation, sub-

sidiary corporate structure was not separate entity for purpose of taxation, and its losses or gains could be considered as losses or gains of title insurance company."

In the course of its opinion the Court stated in part as follows:

* * * * *

"The principle that substance and not form should control in the application of income tax law is fundamental. Fictional corporate camouflage cannot be made the device to escape taxation. On the other hand, equal equity demands that the creation of a subsidiary corporate structure with no purpose of evading tax but solely for the purpose of meeting the exigencies of a serious and possible fatal financial situation should not be regarded as the birth of a new entity completely unidentified with the former for taxing purposes, particularly under the peculiar circumstances surrouning the instant case."

* * * * *

We think that the decision of the Court below is in conflict with the decision of the Third Circuit in *North Jersey Title Ins. Co. et al.* v. *Commissioner of Internal Revenue, supra.* Furthermore the decision of the Court below appears to be in conflict with its own decision in *Munson S.S. Line* v. *Commissioner,* 77 F. (2d) 849 (C. C. A. 2). That case involved a statutory relief provision and the Court held that substance and not form should control and that corporate entities should be disregarded.

The decision of the Circuit Court is also in direct conflict with the decision of the Fourth Circuit in *United States* v. *The Brager Building & Land Corporation, supra,* and the cases cited therein.

This Court has held on several occasions that in tax cases the separate identity of corporations may be disregarded. *Southern Pacific Co.* v. *Lowe,* 247 U. S. 330, 38 S. Ct. 540, 62 L. Ed. 1142; *Gulf Oil Corp.* v. *Lewellyn,* 248 U. S. 71, 39 S. Ct. 35, 63 L. Ed. 133; *New Colonial Ice Co.* v. *Helvering,*

292 U. S. 435, 54 S. Ct. 788, 78 L. Ed. 1348; *Griffiths* v. *Commissioner, supra.*

The case of *Abrams Sons Realty Co.* v. *Commissioner of Internal Revenue,* 40 B. T. A. 653, illustrates the point and presents a situation where the respondent proceeded on a theory exactly opposite to his action in the case at bar. There property was conveyed to a corporation for the benefit of the creditors of the transferors and to permit the corporation to receive the proceeds of a pending condemnation proceeding and to distribute these proceeds to the creditors. The Commissioner of Internal Revenue taxed the corporation as the owner of the property and the recipient of the gain from the condemnation proceeding. The Board overruled the Commissioner and held that the corporation was a mere conduit for the proceeds of the condemnation award and that the original owners of the property (transferred to the corporation) were taxable on the proceeds of the condemnation. The Board relied on the *112 West 59th Street Corporation* v. *Helvering,* 68 F. (2d) 397, and *Central Life Society* v. *Commissioner,* 51 F. (2d) 941.

The Board reached a similar conclusion and disregarded the corporate entities involved in *Moline Properties, Inc.* v. *Commissioner,* 45 B. T. A. No. 105 (November 7, 1941); *J. L. McInerney* v. *Commissioner,* 29 B. T. A. 1, affirmed 82 F. (2d) 665; *Mark A. Mayer,* 36 B. T. A. 117; and *Stewart Forshay,* 20 B. T. A. 537.

The term "controlled" is defined by Article 45-1 of Respondent's Regulations 94, promulgated under the Revenue Act of 1936 as follows:

> "(3) The term 'controlled' includes any kind of control, direct or indirect, whether legally enforceable, and however exercisable or exercised. It is the reality of the control which is decisive, not its form nor the mode of its exercise. A presumption of control arises if income or deductions have been arbitrarily shifted.
>
> "(4) The term 'controlled taxpayer' means any one of two or more organizations, trades, or businesses

owned or controlled directly or indirectly by the same interests.

"(5) 'Group' or 'group of controlled taxpayers' means the organizations, trades, or businesses owned or controlled by the same interests. * * *"

Therefore, under the respondent's own published definition of the term "controlled", the Gold Street Corporation was controlled by the petitioner inasmuch as the stock of both corporations was owned in equal proportions by the same stockholders and the officers and directors of both corporations were identical.

Corporations are even deemed to be affiliated for the purpose of consolidated returns if substantially all of the stock of two or more domestic corporations is owned or controlled by the same interests. *Handy & Harman* v. *Burnet*, 52 S. Ct. 21, 284 U. S. 136. Here, as the Circuit Court found (R. 70), there was a complete stock ownership in all of the corporations involved by four individuals in equal proportions. We believe that the decision of the Court below is out of line with and in conflict with the decisions hereinabove set forth. The doctrine of *Higgins* v. *Smith, supra*, should not be extended to a situation involving a relief provision and relief denied because title to replacement property is taken in the name of a corporation owned and controlled by the same interests as the corporation which received the award.

(c) The attention of the Court is respectfully directed to the fact that the Court below was in doubt on the question whether corporate entity should be disregarded here for the Court said (R. 71):

"* * * But even if it be assumed that the various intercorporate transactions we have mentioned were illusory (see *United States* v. *Brager Building & Land Corporation*, 125 F. (2d) 349, 351), and that Gold Street Corporation was a sham or a mere passive trustee for Vim Securities, still the latter cannot be said to have complied with Section 111(f) of the Revenue Act of 1936, for it did not 'forthwith' expend its award

> in the acquisition either of the Gold Street property or of the control of Gold Street Corporation. * * * "

We think that it is clear from the record that the petitioner did "forthwith" expend the award money in connection with the acquisition of the Gold Street property to replace the Concord Street property condemned. The Court below found as a fact that title passed to the City of New York on June 28, 1935 by reason of the condemnation and that on August 19, 1935 a contract was executed for the purchase of the Gold Street property to replace the property condemned (R. 68). The initial payment of $2,000 was made by the petitioner corporation and the balance of the $10,000 down payment for the property, $8,000, was advanced by the Vim Electric Company in the Fall of 1935. On November 27, 1935 the petitioner delivered its check for $8,000 to Vim Electric in order to refund the latter's advance of $8,000 (R. 68-69). Also a further payment to Vim Electric was made by the petitioner on January 29, 1936. It is true that the balance of the purchase price was advanced by the Vim Electric Company (R. 68-69), but the award was not received by petitioner until the Fall of 1936, over a year after the original condemnation. Although the award was not received for more than a year the property condemned was immediately replaced and after the award was received the creditor, Vim Electric Company, was paid off in monthly installments beginning in January of 1937.

Here again we believe that the relief provisions should be liberally rather than strictly construed and that the condemned property was "forthwith" replaced and payments to the advancing creditor were "forthwith" made after the receipt of the award within the meaning of the statute.

We cannot find that the meaning of the term "forthwith" has been defined by the Courts with relation to Section 112(f) of the Revenue Act of 1936. However, the term has been defined by the Board of Tax Appeals in the leading case decided by the Board on this particular relief provision of the statute, *Washington Railway & Electric Co.* v. *Commis-*

sioner, 40 B. T. A. 1229. In that case at page 1258 of 40 B. T. A. the Board stated:

> "* * * Even though we consider the situation here covered by that part of the statute having to do with the conversion of the property into money which is forthwith expended in the acquisition of similar property, we can see no reason compelling us to make so illiberal a construction of the statute as to conclude that the relief provided by it and intended by Congress is not available to petitioner. To do so it would be necessary to construe the word 'forthwith' as meaning 'afterwards,' that is, after the actual conversion and the receipt of the award. The dictionary defines 'forthwith' as follows: Immediately; without delay; directly; hence, within a reasonable time under the circumstances of the case; promptly and with reasonable dispatch. According to this definition it seems apparent that Congress, by the use of the word 'forthwith,' meant to provide that the expenditure of money resulting from the involuntary conversion of property in the acquisition of similar property must be made with some immediate chronological relationship to the conversion thereby guarding against such a long delay *after* the conversion as to raise a doubt whether the purchase of similar property was actually and in good faith a replacement, or was an additional investment. If there is that immediate chronological relationship between the expenditure for replacement and the condemnation or threat thereof, it is immaterial that the expenditure for replacement immediately preceded the payment of the compensation or immediately followed it. Upon this general subject see *August Buckhardt*, 32 B. T. A. 1272; *M. J. Caldbeck Corporation*, 36 B. T. A. 452. * * *"

The Court below found (R. 70) that the replacing property was acquired for use similar to that of the property condemned and we respectfully submit that the action of the petitioner was in accord with the meaning of the word "forthwith" as that term has been defined by the Board of Tax Appeals in a liberal construction of the statute.

The substance of the petitioner's position is that a relief provision of this character should be liberally construed and that the Court below erred by its strict construction and the resolving of all doubts against the taxpayer.

II.

THE DECISION OF THE COURT BELOW THAT THE PETITIONER WAS "CARRYING ON OR DOING BUSINESS" DURING THE YEAR 1936 IS NOT IN ACCORD WITH DECISIONS OF THIS COURT AND IS IN CONFLICT WITH DECISIONS OF THE OTHER CIRCUIT COURTS OF APPEAL.

Section 105(a) of the Revenue Act of 1935, as amended by Section 401 of the Revenue Act of 1936 provides for a capital stock tax on all domestic corporations with respect to carrying on or doing business.

Section 106 of the Revenue Act of 1935 as amended by Section 402 of the Revenue Act of 1936 imposes an excess profits tax on every corporation which is subject to capital stock tax.

Accordingly, the test for the imposition of an excess profits tax is whether a corporation is "carrying on or doing business."

It appears well settled that a corporation which merely receives the income earned by its assets which it owns and distributes that income among stockholders is not "engaged in or doing business." *Zonne* v. *Minneapolis Syndicate,* 220 U. S. 187, 31 S. Ct. 361, 55 L. Ed. 428; *McCoach* v. *Minehill, etc. R. Co.,* 228 U. S 295, 32 S. Ct. 842, 56 L. Ed. 1269; *U. S.* v. *Emery, etc. Co.,* 237 U. S. 28, 35 S. Ct. 499, 59 L. Ed. 825; *Rose* v. *Nunnally Investment Company,* 22 F. (2d) 102 (C. C. A. 5). The mere ownership and leasing, without operation of a parcel of real estate is not such a transaction of business as to subject the owner to excess profits tax. *Sears* v. *Hassett,* 111 F. (2d) 965 (C. C. A. 1); *Kingkade Hotel Co.* v. *Jones,* 30 F. Supp. 508.

In *Zonne* v. *Minneapolis Syndicate, supra,* this Court stated in part as follows:

> "The corporation involved in the present case, as originally organized, and owning and renting an office building, was doing business within the meaning of the statute as we have construed it. Upon the record now presented we are of opinion that the Minneapolis Syndicate, after the demise of the property and reorganization of the corporation, was not engaged in doing business within the meaning of the act. It had wholly parted with control and management of the property; its sole authority was to hold the title subject to the lease for 130 years, to receive and distribute the rentals which might accrue under the terms of the lease, or the proceeds of any sale of the land, if it should be sold. The corporation had practically gone out of business in connection with the property, and had disqualified itself by the terms of reorganization from any activity in respect to it."

The record herein clearly shows that the taxpayer's building was condemned in 1935 and that in 1936, the year here involved, the taxpayer received the award and merely passed the award money on to its tenant for money advanced to replace the building originally owned. The Court below held that the taxpayer should be deprived of the benefits of Section 112(f) because the building purchased in replacement was purchased in the name of another corporation. Thus, under the Court's decision on the relief point, the petitioner herein did not even own a building in 1936. It became merely an empty shell, neither owning nor operating property.

The attorney fees of $2,050.39, expended by the petitioner in 1936, were paid to the attorney who represented the petitioner in the condemnation proceedings (Petitioner's Exhibit 2). So it becomes clear that the attorney fees were not in connection with the operation of the corporation as a going business but rather were fees which were incurred in the very proceeding which depleted the petitioner of its real property.

It is therefore respectfully submitted that the decision of the Court below is not in accord with the decisions of this Court in *Zonne* v. *Minneapolis Syndicate, supra; McCoach* v. *Minchill, supra* and *U. S.* v. *Emery, supra.* Also the decision is in conflict with the decisions of the Fifth Circuit in *Rose* v. *Nunnally Investment Company, supra,* and the First Circuit in *Sears* v. *Hassett, supra.*

III.

THE CIRCUIT COURT OF APPEALS HAS DECIDED AN IMPORTANT QUESTION OF FEDERAL TAX LAW WHICH HAS NOT BEEN BUT SHOULD BE SETTLED BY THIS COURT.

The relief provisions of Section 112(f) of the 1936 Act and the similar provisions of other Revenue Acts have, as pointed out hereinabove, been considered on numerous occasions by the Board of Tax Appeals. However, there have been few Court decisions upon the subject and the questions involved therein have never been passed upon by this Honorable Court. We have demonstrated hereinabove that the relief provisions of Section 112(f) of the 1936 Act, involving condemnation awards should be construed liberally rather than strictly as was done by the Court below.

The attention of this Court is respectfully directed to the fact that in denying the relief provisions of the pertinent section of the statute to the petitioner, the Circuit Court of Appeals relied on the doctrine of *Higgins* v. *Smith, supra.* We think that it is important that this Court settle the question whether the doctrine of *Higgins* v. *Smith, supra,* should be extended and applied to such circumstances as are here involved and where relief provisions are to be interpreted. Compare *Griffiths* v. *Commissioner, supra,* and *United States* v. *The Brager Building & Land Corporation, supra.*

It also appears that on the issue involving the question whether the petitioner was "doing business" the decision of

the Court below stands practically alone on this important matter. We think it clear that if the corporation is to be denied relief under Section 112(f) on the theory that the Gold Street property was not purchased in its name, then certainly it cannot be said that the petitioner was doing business within the taxable year after having been deprived of its holdings by reason of the condemnation proceedings.

It is therefore respectfully submitted that the petition should be granted.

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